Free trade and costly love

By Robert Skidelsky
January 20, 2014 – *Project Syndicate*

The World Trade Organization's ministerial conference in Bali in December produced a modest package of encouragements to global trade. More broadly, the WTO's multilateral approach has shown its worth by preventing a massive increase in trade barriers, unlike in 1929-1930, when protectionism helped deepen and broaden the Great Depression. But the main question – whether globalization is a good thing, and for whom – remains unanswered.

The essence of globalization – free trade – rests on the theory of comparative advantage, which views international trade as profitable even for a country that can produce every commodity more cheaply (in terms of labor or all resources) than any other country.

The textbook example given by the Nobel laureate Paul Samuelson is that of a town's best lawyer who is also its best typist. Provided that he is better at law than at typing, he should specialize in law and leave his secretary to do the typing. That way, both of their earnings will be higher.

The same logic applies to countries. Each country should specialize in producing those things that it produces most efficiently, rather than producing a bit of everything, because that way its income will be higher.

Economists regard understanding the theory of comparative advantage as a test of professional competence. But are the incompetents – say, the average person who believes that buying cheap imports from China destroys Western jobs – always wrong?

Samuelson, who called the theory of comparative advantage the most beautiful thing in economics, changed his tune a bit at the end of his life. Free trade, he said, works fine with unchanging technology. But if countries like China can combine Western technology with low wages, then trade with China will lower Western wages. True, the West will be able to get its goods more cheaply; but, as Samuelson put it, "being able to purchase groceries 20% cheaper at Wal-Mart does not necessarily make up for the wage losses."

Nor, he might have added, would being able to buy goods more cheaply compensate for many other good things in life that are sacrificed to efficiency. The argument for free trade is an argument for welfare, but welfare defined exclusively in terms of money. Time is money: the more money you can squeeze out of an hour's work, the better off you are. But what about all of the things that you enjoy doing, or that you think of as valuable, that do not maximize your earnings?

The economist responds that the more efficient you are at your work, the more time you will have for those other things. The trouble is that the more you start to think of your welfare in terms of money, the more likely you are to regard spending time with your friends or making love as an "opportunity cost" – the loss of money you would have made by working instead – rather than a benefit.

The goal of squeezing as much money as possible out of time makes a great deal of sense in poor countries, where inefficient use of time can lead to starvation. The whole point of economic development is, surely, to reduce the cost of inefficiency. Yet economists, not noticing that their logic is less applicable to rich countries, continue trying to extend it to more and more areas of life.

A newly luxuriant research area is "life outsourcing." Paying someone else to fold your socks is a way to maximize your own earnings and those of the sock folder. Even as penniless graduate students, the economists Jon

Steinsson and Emi Nakamura borrowed money to pay people to do their household chores, calculating that "spending an extra hour working on a paper was better for their lifetime expected earnings than spending that same hour vacuuming."

Likewise, the economists Betsey Stevenson and Justin Wolfers, pioneers of "lovenomics," cite the tax code as a reason for not marrying. They also conducted a cost/benefit analysis before having a child. As Wolfers explains,

"The principle of comparative advantage tells us that gains from trade are largest when your trading partner has skills and endowments that are quite different from yours. I'm an impractical bookish Harvard-trained empirical labor economist, while Betsey is an impractical and bookish Harvard-trained empirical labor economist. When your skills are so similar, the gains from trade aren't so large. Except when it comes to bringing up our baby. There, Betsey has a pair of, um, endowments that mean that she's better at inputs. And that means that I'm left to deal with outputs."

As Stevenson helpfully clarifies, "it turns out that fathers can be pretty good at dealing with diapers."

At this point, those untutored in economics are likely to start gnashing their teeth. "I enjoy doing lots of things that do not maximize my earning power," they might protest. But as soon as we accept the premise that to be rational is to seek to maximize one's utility – defined in terms of consumption, with money the way to maximize it – the economist's logic wins.

At that point, we must admit that it is *irrational* to spend time on long conversations with friends if it is time stolen from inventing, say, new software (unless the conversation helps the invention). For Wolfers, it is a coincidence that what earns him the most money, economics, is also what he most enjoys doing.

Such reasoning crystallizes opposing views of the world, one in which time is a cost, and the other in which it is a benefit. The first sees time spent on enjoyment as a missed opportunity; the second as part of the good life. We should be clear about what is at stake in the choice between the two.

Robert Skidelsky, Professor Emeritus of Political Economy at Warwick University and a fellow of the British Academy in history and economics, is a member of the British House of Lords.